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Principle of 'Preponderance of Probability' Inequitable to the norm of Pre-Existing Disputes under IBC, 2016

Rajratan Babulal Agarwal v. Solartex India Pvt. Ltd. & Ors.

Citation	2022 SCC OnLine SC 1395
Date	13 October 2022
Court	Supreme Court of India
Coram	Hon'ble Justice K.M. Joseph Hon'ble Justice Hrishikesh Roy

1. Factual Matrix & Procedural History:

- 1.1 Agreements were entered between Solartex India Pvt. Ltd. (“**Respondent No. 1/Operational Creditor**”) and Honest Derivatives Pvt. Ltd. (“**Respondent No. 2/Corporate Debtor**”) for the purpose of supply of coal, which was to be used in boilers that manufacture starch and allied products. After some time, the Corporate Debtor directed the Operational Creditor to discontinue the supply of coal, as the coal did not conform to the terms of the purchase order.
- 1.2 On 03.02.2018, the Operational Creditor issued a demand notice to the Corporate Debtor under the Insolvency and Bankruptcy Code, 2016 (“**IBC**”) and raised a claim for Rs 21,57,700:38/- inclusive of interest. The Corporate Debtor responded to the Demand Notice, and in turn demanded a total amount of Rs.4.44 crores from Operational Creditor, as damages towards the supplied coal not being of the promised quality. Thereafter, the Corporate Debtor also filed a civil suit against the Operational Creditor claiming damages.
- 1.3 That the Operational Creditor had filed a petition under Section 9 of IBC, seeking initiation of Corporate Insolvency Resolution Process (“**CIRP**”) against the Corporate Debtor. The NCLT initiated CIRP against the Corporate Debtor vide order dated 28.05.2020 upon the premise that there was no pre-existing dispute. Pursuant to that the ex-Director of the Corporate Debtor namely Mr. Rajratan Babulal Agarwal (“**Appellant**”) went in appeal before the NCLAT contending that there was a pre-existing dispute, wherein the appeal was dismissed. Thereafter, aggrieved by the order the Appellant filed a second appeal before the Supreme Court.

2. Issue(s):

- 2.1 Whether the Appellant’s dispute which can be described as ‘a pre-existing dispute’ as understood in Mobilox Innovations Private Limited v. Kirusa Software Pvt. Ltd.¹?

3. Contentions of the Parties:

- 3.1 The Appellant argued that in a contract of sale of goods, a term may be a condition or a warranty. The Appellant had elected to treat the condition relating to the quality of the goods as a warranty.
- 3.2 On the other hand, the Operational Creditor contended that the Appellant had written merely three emails before issuing the Demand Notice and none of those emails raised any dispute. Further, the Corporate Debtor continued to consume the goods supplied even after the alleged deficiency continued to exist.

4. Judgment:

- 4.1 In the present matter, Section 55(2) of the Act spoke about a certain date which must be fixed in the contract. The clause in the purchase order refers to payment of the price being affected within seven days of delivery. It could, no doubt, be said that the date of payment cannot go beyond a period of seven days at any rate of the delivery, and therefore, the seventh day could be treated as a day which was certain.
- 4.2 The Court opined that the buyer could lean on Section 59 and set up a breach of warranty and seek at least the diminution of the price if not extinction of the same
- 4.3 The Bench observed that on 30.10.2016 an email was sent to the Operational Creditor by STDPL, which is a sister-concern of the Corporate Debtor, by making express reference to Corporate Debtor. The said email raised issues relating to the quality of the coal and

¹ (2018) 1 SCC 353.

- pictures were attached for reference. The Bench opined that the NCLT had erred in not taking the said email into consideration while determining existence of dispute.
- 4.4 While placing reliance on the Mobilox² judgment, it was observed that IBC does not enable the Operational Creditor to put the Corporate Debtor into insolvency resolution process prematurely over small amounts of default. It is for this reason that it is enough that a dispute exists between the parties.
 - 4.5 The Bench opined that, *“The standard, in other words, with reference to which a case of a pre-existing dispute under the IBC must be employed cannot be equated with even the principle of preponderance of probability which guides a civil court at the stage of finally decreeing a suit Once this subtle distinction is not overlooked, we would think that the NCLT has clearly erred in finding that there was no dispute within the meaning of the IBC.”*
 - 4.6 The contention that no debit note was raised in respect of supplied goods and that the accounts may not bear out the case of the Appellant about the alleged loss, it was the Court’s opinion, that while they may have lent assurance to the Corporate Debtor but their absence would not absolutely rule out the existence of a ‘pre-existing dispute’ under the IBC.
 - 4.7 The Bench further observed that it cannot be oblivious to the limited nature of examination of the case of the Corporate Debtor projecting a pre-existing dispute. Overlooking the boundaries of the jurisdiction can cause a serious miscarriage of justice besides frustrating the object of the IBC.

5. PSL Opinion:

- 5.1 The Supreme Court in his Judgment held that NCLT had erred in its finding that there was no pre-existing dispute. It also opined that since Section 13 of the Act permits the buyers to waive a condition and so it will be open to the first respondent to canvass that at any rate the second respondent has waived the alleged condition. It would have been extensively unfair if the appeal would not have been allowed and the NCLT judgment would have been upheld. Accordingly, the Court was correct in rejecting the petition under Section 9 of IBC.

² Ibid.